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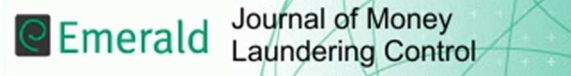
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Implementation of the Concept of 'Politically Exposed Persons (PEPs)' in India

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Review

Implementation of the Concept of ‘Politically Exposed Persons (PEPs)’ in India

Purpose: The purpose of this paper is to critically examine the concept of ‘Politically Exposed Persons (PEPs)’ as provided under the Indian AML regime, particularly focussing on the Reserve Bank of India (RBI) guidelines to its supervised banks on dealing with the potential money laundering risks posed by PEPs.

Design/Methodology/approach: The definition of PEPs as provided by international standard setters, and the concept as defined by the Indian AML regime was examined to examine the extend of the compliance of the Indian AML regime with the mandatory requirements of revised 2012 FATF recommendations and other international standards.

Findings: The paper clearly establishes that the current AML regime of India does not fully comply with the mandatory requirements of the revised 2012 FATF recommendations, nor do the RBI guidelines provide any clear indications to its supervised banks on the effective development and implementation of AML PEPs controls. The paper argues that it is high time for India to increase its regulatory focus on the issue of PEPs and to expand its definition of PEPs by including both domestic PEPs and ‘close associates’ of PEPs within the definition.

Originality: The paper demonstrates in an exceptional way that despite variations in the scope of the PEPs definition at international level, all the standard setters have included certain key individuals (both domestic and foreign PEPs as well as ‘close associates’ of PEPs) within the scope of the definition and how the legal and regulatory requirements in India are falling short of compliance even with these minimum key requirements. By adopting a step-by-step approach in critically examining the current legal and regulatory requirements enforced on banks in India to efficiently deal with the money laundering risks posed by PEPs, the paper makes a valuable contribution in highlighting the steps that might be taken to strengthen PEPs AML controls in India.

Keywords: Money Laundering, politically exposed persons, , financial institutions, banks, Reserve Bank of India, PEPs

INTRODUCTION

In the Mutual Evaluation Report (MER) of India, which was adopted by the Financial Action Task Force (FATF) on 24 June 2010, it was reported that the preventive measures in place in India at that time to deal with the money laundering risks posed by Political Exposed Persons (PEPs) were inadequate and needed to be strengthened.¹ In MER 2008, India was rated to be ‘Partially Compliant (PC)’ with Recommendation 6 of the 2003 FATF Recommendations (hereinafter ‘old FATF Recommendations’). The major shortcomings in the Indian AML law

¹ Financial Action Task Force (FATF), *Mutual Evaluation Report Executive Summary: Anti-Money Laundering and Combating the Financing of Terrorism – India* (25 June 2010).

and regulations were identified to be the lack of requirement by the Reserve Bank of India (RBI) circulars (a) to implement on-going risk management procedures for identifying PEPs, and (b) to apply enhanced measures to close relatives of PEPs.²

Later, however, in the 8th Follow-up Report of India published in June 2013, which is a report on the progress made by India in implementing the AML measures and addressing the deficiencies identified in MER 2008, it was concluded that India has achieved sufficient level of compliance with old FATF Recommendation 6 by addressing nearly all the deficiencies earlier reported with regard to PEP provisions under Indian law.³ India's current level of compliance was thus raised to be equivalent to 'Largely Compliant (LC)' with respect to PEP provisions. This was as a result of RBI's circular issued on 9 June 2010 which required banks (a) to implement on-going risk management procedures for identifying PEPs and accounts for which a PEP may be the beneficial owner, and (b) to apply enhanced due diligence measures to close relatives (but not close associates) of PEPs.

It is worth noting that the 8th Follow-up Report of India 2013 was based on the compliance of Indian AML law and regulations with the old FATF Recommendations. The FATF has significantly revised its provisions relating to PEPs in its 2012 revision (hereinafter 'revised' FATF Recommendations) and Recommendation 12 and 22 of the revised FATF Recommendations now deal with money laundering measures that should be applied to PEPs. Arguably, the revision of old FATF Recommendation 6 was mainly motivated by the desire to prevent grand corruption by public officials by making laundering of the criminal proceeds more difficult. In a joint paper published by the United Nations Office of Drug and Crime (UNODC) and the World Bank in 2007, it was estimated that the corrupt money received by public officials in developing and transition countries ranges from \$20 billion to \$40 billion per year – a figure equivalent to the annual GDP of the world's 12 poorest countries.⁴ From the money laundering perspective, the issue of PEPs is arguably the most important point of intersection between anti-money laundering and anti-corruption efforts. Consequently, the provisions relating to PEPs in the revised FATF Recommendations were made stricter, requiring countries to implement an effective PEP regime (which complies with Recommendations 12 and 22) to enable them to efficiently identify these higher risk individuals and to better monitor their transactions, and thereby, to effectively combat any money laundering risks posed by PEPs.

The revised FATF Recommendations were issued around four years ago, in February 2012. After June 2013, India was removed from the FATF's regular follow-up process.⁵ Nonetheless, the country is still subject to the peer review 'mutual evaluation' process of the FATF where its compliance with FATF's revised recommendations will be assessed. This paper examines the current level of compliance of Indian law and regulations with the revised

² Ibid 17.

³ FAFT, *Mutual Evaluation of India: 8th Follow-Up Report* (June 2013).

⁴ UNODC and the World Bank, *Stolen Asset Recovery (StAR) Initiative: Challenges, Opportunities and Action Plan*. (The World Bank 2007).

⁵ India was removed from the regular follow-up process in June 2013 on the grounds that it has achieved sufficient progress for all core and key FATF Recommendations. Till June 2013, India reported back seven times to FATF regarding its progress on the implementation and strengthening of its AML/CFT measures.

FATF Recommendations, with particular focus on PEPs, and makes a strong case for an amendment to the Indian AML regime to expand the definition of PEPs and for the issuance of clear guidelines by RBI on the concept of PEPs. The paper argues that such an amendment and actions are imperative not only to comply with the revised FATF Recommendations but also to mitigate the potential money laundering risks posed by domestic PEPs to the Indian economy, which arguably would be devastating and significant in light of the scale of grand corruption in India and the gross abuses of corrupt PEPs in the past few years.

Overview of AML Framework in India

The cornerstone of the relevant AML framework in India is the Prevention of Money Laundering Act 2002 (PMLA), which came into force on 1 July 2005. The most significant amendments that PMLA 2002 subsequently underwent were in 2009 (regarding the criminalisation of terrorist financing offence and extension of the list of predicate offences with cross-border implications) and in 2012 (regarding the expansion of the definition of money laundering to include cheating, concealment, acquisition, use and possession of proceeds of crime within its scope; and the requirement for Know Your Customer (KYC) obligations to include of ‘beneficial ownership’ during KYC measures for reporting entities).

RBI is the authority responsible for supervising banking institutions and compliance with the legislative framework on the prevention and suppression of money laundering and terrorist financing (PMLA) by the institutions supervised by it. RBI regularly issues AML/CFT guidelines to banks and financial institutions (in the form of circulars) to prevent the Indian financial system from being used, intentionally or unintentionally, by criminal elements for laundering money or terrorist financing activities.

RBI, in the context of its supervisory tasks, checks supervised institutions’ compliance with their AML/CFT-related obligations and assesses the adequacy and effectiveness of their AML/CFT procedures. It should be pointed out that the RBI has no power to conduct preliminary investigations or to examine in substance suspicious transaction reports submitted by supervised institutions. These powers are reserved to the Financial Intelligence Unit of India (FIU-India), the law enforcement or judicial authorities, as appropriate.

FIU-India was established in November 2004 by the national government as the central national agency responsible for receiving, processing, analysing and disseminating information relating to suspicious financial transactions. FIU-India is also responsible for coordinating and strengthening efforts of national and international intelligence, investigation and enforcement agencies in pursuing global efforts against money laundering and related crimes. It is an independent body reporting directly to the Economic Intelligence Council (EIC) headed by the Finance Minister.

PEPs: How the concept has been defined at International Level

International standard setters agree that PEPs include natural persons who are or have been entrusted with prominent public functions. Sadly, however, despite this agreement, there is a lot of inconsistency in the terminology used and in the scope of the PEPs definition, as well

as the underlying requirements in the international standards, interpretive notes and methodologies. Some of the key inconsistencies that exist are highlighted in Table 1 below, which arguably have created a lot of confusion as to the concept of PEPs and thus hinder its effective implementation.

Table 1: Definition of PEPs by different International Standard Setters and Regulatory Authorities

International standard setters and Regulatory Authorities	Whether PEPs definition includes domestic or foreign PEPs or both?	Whether the definition includes 'close family' or 'close associates' or both?	Are there any other categories included in the definition of PEPs?
Revised FATF Recommendations ⁶	Includes both domestic and foreign PEPs, but EDD measures are required for domestic PEPs only in cases of a higher risk business relationship with them.	Includes close family, but no limitation on the degree of relationship; for instance, immediate or extended family; Includes close associates, which means individuals who are closely connected to a PEP, either socially or professionally.	Includes international organisation PEPs
United Nations Convention Against Corruption (UNCAC) ⁷	Includes both domestic and foreign PEPs	Includes family members, but no limitation on the degree of relationship; for instance, immediate or extended family; Includes close associates but the term is defined to include both companies and natural persons.	
The 4 th EU Money Laundering Directive ⁸	Includes both domestic and foreign PEPs. ⁹	Includes family members, but the definition focuses only on immediate family members (i.e.,	Includes deputy or assistant ministers; members of governing bodies of

⁶ The Old FATF Recommendations do not include 'domestic PEPs' within the definition of PEPs. The old FATF Recommendations 'Glossary of Definitions used in the Methodology' simply defines PEPs as 'individuals who are or have been entrusted with prominent public functions in a foreign country, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state owned corporations, important political party officials. Business relationships with family members or close associates of PEPs involve reputational risks similar to those with PEPs themselves. The definition is not intended to cover middle ranking or more junior individuals in the foregoing categories.'

⁷ United Nations Office on Drugs and Crime (UNODC), United Nations Convention Against Corruption (New York 2004) Art. 52.

⁸ Directive 2015/849 of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC [2015] OJ L141/73.

⁹ Under the 3rd EU Money Laundering Directive, the term PEPs has been defined to include both foreign and domestic PEPs, EDD measures were only required to be applied to foreign PEPs (See, Council Directive

		spouse, children and their spouses, and parents of PEPs). Includes close associates, but only 'persons known to be close associates', ¹⁰ which means natural persons.	political parties; ambassadors; high-ranking officers in armed forces; members of administrative, management and supervisory bodies of state-owned enterprises; international organisation PEPs; members of courts of auditors or of the boards of central banks.
The Wolfsberg Group ¹¹	Includes both domestic and foreign PEPs	Includes close family members, but the definition focuses only on immediate family members (i.e., spouse, children, parents and siblings of PEPs). Includes close associates, but focuses particularly on PEP's widely- and publicly-known close business colleagues and/or personal advisors, in particular, financial advisors or persons acting in a financial fiduciary capacity.	Includes heads and senior officials in the armed forces, members of ruling royal families with governance responsibilities, senior executives of state-owned enterprises and senior officials of major political parties.
Basel Committee on Banking Supervision ¹²	Includes both domestic and foreign PEPs	Does not use the terms 'close family' or 'close associates', but broadly includes close persons or companies clearly related to PEPs.	

It thus becomes apparent from Table 1 that the PEP provisions are not uniform in scope across standard setters and this might have arguably resulted in a lot of inconsistency regarding the concept of PEPs in the AML regimes of different jurisdictions. Nonetheless, one thing that becomes evident from the above analysis is that despite variations in the scope of the PEP definition, all the standard setters have included within the scope of the definition both domestic and foreign PEPs, requiring countries to ensure that their financial institutions consider PEPs to be high-risk customers and, accordingly, implement procedures for their

2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing [2005] OJ L309/15).

¹⁰ The term 'persons known to be close associates' has been defined under Art. 3(11) of the 4th EU Money Laundering Directive to mean: '(a) natural persons who are known to have joint beneficial ownership of legal entities or legal arrangements, or any other close business relations, with a politically exposed person;(b) natural persons who have sole beneficial ownership of a legal entity or legal arrangement which is known to have been set up for the de facto benefit of a politically exposed person.'

¹¹ The Wolfsberg Group, *Wolfsberg Frequently Asked Questions (FAQ's) on Politically Exposed Person ("PEPs")* <[http://www.wolfsberg-principles.com/pdf/faq/Wolfsberg_PEP_FAQs_\(2008\).pdf](http://www.wolfsberg-principles.com/pdf/faq/Wolfsberg_PEP_FAQs_(2008).pdf)> accessed 25 December 2015.

¹² Basel Committee on Banking Supervision, *Customer Due Diligence for Banks* (October 2001).

identification, with enhanced due diligence procedures at account opening, on-going monitoring and reporting of suspicious transactions.

Even the revised FATF Recommendations require countries to have appropriate risk management systems in place to identify whether their customers or beneficial owners are foreign, domestic or international organisation PEPs. FATF recommendations require that for foreign PEPs, EDD measures must be applied, whereas for domestic and international organisation PEPs, the nature and extent of due diligence should depend upon the risk perceived by the bank in establishing a business relationship with such PEPs. In assessing its risk, the bank, for instance, should take into account the risk posed by the product, service or transaction sought, as well as other factors that have a bearing on money laundering and corruption risks. Where there is a higher risk, the AML/CFT approach should be stricter by accordingly, i.e., applying EDD measures even to domestic and international organisation PEPs. In addition, it has also been recommended by the revised FATF recommendations that the regulatory authorities of a country should provide appropriate guidance to banks in this regard.

PEPs: How the concept is defined under the Indian AML regime

In India, RBI defines PEPs as

individuals who are or have been entrusted with prominent public functions in a foreign country e.g., Heads of States or of Governments, senior politicians, senior government/judicial/military officers, senior executives of state owned corporations, important political party officials etc. ... [PEP] norms *may also be applied* to the accounts of the family members or close relatives of PEPs.¹³

Arguably, the above RBI definition of PEPs clearly establishes two points: first, RBI did not go deep into the question of properly defining the scope of the concept of PEPs. This becomes apparent from the use of the word 'etc.' in the definition, which is a very broad expression with no clearly defined boundaries. It arguably creates uncertainty and ambiguity in the scope of the definition of PEPs and consequently impedes the effective development and implementation of PEPs provisions and controls in the jurisdiction. Secondly, by use of the wording 'PEP norms may be applied to ... the family members or close relatives of PEPs', RBI suggests that it is left entirely to the discretion of the banks whether or not to apply EDD measures to the family members or close relatives of PEPs, which arguably does not fully comply with the revised FATF Recommendations, as these require financial institutions to apply similar EDD measures to PEPs, their family members and close associates.¹⁴

¹³ Reserve Bank of India (RBI), *Master Circular – Know Your Customer (KYC) norms/Anti-Money Laundering Standards (AML)/ Combating of Financing of Terrorism (CFT)/Obligation of Banks under PMLA 2002* (Master Circular – DBOS.AML.BC.No. 24/14.01.001/2013-14, July 1, 2013), 8

¹⁴ FATF, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation* (February 2012), Recommendation 12.

Moreover, in an RBI circular dated July 1, 2013, it was specifically stated that ‘if banks consider necessary, PEPs *may be categorised* as higher risk customers requiring higher level of monitoring.’¹⁵ Arguably, this wording appears to be giving discretion to the banks whether or not to consider PEPs as higher risk customers, depending upon the risk assessment of the customer after taking into account different factors. To the contrary, however, the FATF Recommendations, both old and revised, always designate PEPs as a special category of customers posing high risk for money laundering. Once the risk management system of the bank identifies a person to be a PEP, the FATF requires banks to always consider such individuals as high risk customers, which somehow contradicts the above wording of the RBI circular. Nevertheless, the same circular later provides that customers requiring higher due diligence include ‘politically exposed persons (PEPs) of foreign origin, customers who are close relatives of PEPs and accounts of which a PEP is the ultimate beneficial owner.’¹⁶ Certainly, this wording is in compliance with the FATF Recommendations, but it is inconsistent with the former RBI approach where the banks have been given discretion to categorise PEPs as low-, medium- or high-risk customers. Such inconsistency in the guidelines of a regulatory and supervisory body clearly establishes the lack of regulatory focus and significance given to the issue of money laundering risks posed by PEPs in the jurisdiction.

It is noteworthy that despite the lack of clear guidance by RBI to its supervised banks on the concept of PEPs, it, however, requires banks to subject PEPs to EDD measures by requiring them to obtain senior management approval not only for *new* PEP customers identified during account opening but also for *existing* customers that became a PEP. The banks are also required to take reasonable measures to establish the source of wealth, and conduct enhanced on-going monitoring of the business relationship with PEPs, the family members or close relatives (though not close associates) of PEPs, as well as the accounts of which PEP is the beneficial owner.

Certainly, the RBI provisions relating to applying EDD measures to PEPs are in compliance with the FATF Recommendations. However, if we examine only the scope of the definition of PEPs as adopted by RBI, it can be argued that the definition, only to an extent, is in compliance with the old FATF Recommendation 6 (which also primarily focuses on foreign PEPs and recommends that countries apply EDD measures on foreign PEPs, with no clear guidelines on how to deal with domestic PEPs). This definition, however, does not comply with the revised FATF Recommendations (Recommendation 12 and 22), which require countries to make provisions for financial institutions to determine whether a customer or beneficial owner is a domestic PEP and in cases of a higher risk business relationship with such persons, financial institutions are required to apply additional measures consistent with those applicable to foreign PEPs. Moreover, no provision has been made under the Indian AML/CFT regime to deal with the potential money laundering risks posed by ‘close associates’ of PEPs, which is arguably a critical factor to prevent corruption. Even the term ‘close relatives’, as it appears to be understood from the RBI circular, includes only

¹⁵ RBI (n 13) 8.
¹⁶ *ibid* 10.

immediate family members of PEPs, i.e., wife, daughter, son and parents of PEPs,¹⁷ similar, to some extent, to what has been provided under the Wolfsberg Principles and the 4th EU Money Laundering Directive, but limited only to the spouse, children and parents of a PEP. Nonetheless, considering the gravity of the problem associated with grand corruption and money laundering, the question now is whether India needs to expand its definition of PEP to include ‘close associates’ and ‘close family’ (both immediate and extended family) within the definition, which is answered in the affirmative by this paper, especially considering the scale of grand corruption in the jurisdictions (which is discussed below).

Has RBI issued enough guidance to banks regarding PEPs?

In addition to the lack of sufficient compliance of the current RBI guidance with the revised FATF Recommendations on the concept of ‘PEPs’, this paper argues that RBI has also not issued enough guidance to its supervised banks regarding PEPs, despite requiring them to identify PEPs and apply EDD measures to them. For instance, there has been no sufficient guidance provided by the RBI on the following crucial elements relevant to PEPs:

- whether low-ranking officials and public place holders are to be included within the definition of PEP or only ‘senior’ officials;
- whether the definition includes only ‘politicians’ or ‘government officials’ as well;
- what the difference between ‘family members’ and ‘close relatives’ is, as used in the PEP definition;
- what constitutes ‘close relatives’; and
- if there is any timeframe for review of PEP status.

In an AML survey conducted by KPMG in 2012 involving 100 financial institutions (mainly public sector banks, private sector banks, foreign banks, insurance companies and mutual funds) it was reported that only 77 per cent of financial institutions in India have specific procedures in place to identify PEPs (i.e., foreign PEPs).¹⁸ Although this figure appears to be encouraging, it does not lead to any definitive conclusions as to the compliance of the banking sector with the old FATF Recommendations on PEP provisions, for the survey includes only 45 banks as respondents. Moreover, compared to 80% respondents in North America and 77% of respondents in the Middle East and Africa, all of which recognise and distinguish between foreign and domestic PEPs, the recent KPMG Global AML survey reported that the Asia Pacific region, including India, lags far behind in the actual identification and monitoring of PEPs with only 51% respondents actually identifying and distinguishing between foreign and domestic PEPs to apply a risk-based approach.¹⁹ Arguably, in the Indian context, this deficiency could be attributed to both the lack of a uniform definition of PEPs at the international level, as well as to the lack of sufficient

¹⁷ RBI (n 10) [2.4(g)]

¹⁸ KPMG, *India Anti-Money Laundering Survey 2010* <
<https://www.in.kpmg.com/SecureData/aci/Files/IndiaAntiMoneyLaunderingSurvey2012.pdf>> accessed 25 December 2015.

¹⁹ KPMG, *Global Anti-Money Laundering Survey* <
<https://www.kpmg.com/KY/en/IssuesAndInsights/ArticlesPublications/PublishingImages/global-anti-money-laundering-survey-v3.pdf>> accessed 15 December 2015.

guidance from RBI to its supervised institutions on the concept of PEPs, the effective implementation of AML measures relating to PEPs, as well as the adoption of a risk-based approach with regard to the level of due diligence to be performed on domestic PEPs when compared to foreign PEPs.

Furthermore, there also appears to be a lack of regulatory sanctions imposed by RBI on banks for PEPs deficiencies. There has been no reported case in India where the banks have been sanctioned or faced any penalties for not effectively implementing PEP measures and controls, which arguably does not coincide with the KPMG 2012 survey where the majority of financial were reported as not conducting on-going monitoring of their business relationships with PEPs and almost a quarter did not have any specific procedures in place to identify PEPs. Interestingly, however, in the past two years, RBI has fined a number of banks for their general AML deficiencies, which reportedly does not include anything related to PEPs. These banks include, for instance, three major private banks (HDFC, Axis and ICICI – fined Rs. 4.5 crore, 5 crore and 1 crore, respectively in June 2013),²⁰ three public banks (Dena Bank, Oriental Bank of Commerce, and Bank of Maharashtra – each fined Rs. 1.5 crore for violation of KYC AML norms),²¹ and most recently, two co-operative banks (Krishna Mercantile Cooperative Bank (KMCB) and Khargone Nagrik Sahakari Bank (KNSB) – fined Rs. 5 lakh and Rs. 1 lakh, respectively in August 2015).²² However, considering the risks posed by deficient AML controls applied by financial institutions in India, the IMF has rightly noted that ‘the sanctions that supervisors have applied for AML/CFT deficiencies in India cannot be considered to be effective, dissuasive or proportionate.’²³

Moreover, this study further argues that the lack of sanctions or penalties for any reported deficiencies in AML procedures relating to PEPs in the Indian banking sector could have been due to various reasons. First, it could be that the banking institutions have appropriate and effective PEP procedures in place, which arguably does not appear to be the case, as discussed above. Second, the lack of sanctions was potentially a result of PEPs being part of a bank’s wider AML system. Breaches of the PEP obligations were likely to be indicative of more fundamental problems with a bank’s defences and would result in sanctions for overall AML system failures rather than sanctions for PEP breaches. Third, the lack of PEP sanctions may be attributable, in part, to a lack of regulatory focus on PEPs. Arguably, if no sufficient guidance has been provided by the RBI itself to its supervised banks on the concept of PEPs, it would be difficult for it to monitor and require the banks to effectively implement AML-

²⁰ BS Reporter, ‘RBI fines Axis, HDFC & ICICI banks’ *The Business Standard* (New Delhi, 10 June 2013) < http://www.business-standard.com/article/finance/rbi-fines-axis-hdfc-icici-banks-113061000612_1.html> accessed 25 December 2015.

²¹ Reporter, ‘KYC money laundering norms violation: RBI slaps Rs. 1.5 crore fine each on three public banks’ *First Post* (30 April 2015) < <http://www.firstpost.com/business/kyc-money-laundering-norms-violation-rbi-slaps-rs-1-5-cr-fine-each-on-3-public-banks-2219808.html>> accessed 25 December 2015.

²² NDTV, ‘RBI fines 2 Co-operative Banks under Anti-Money Laundering Rules’ *NDTV Profit* (27 August 2015) < <http://profit.ndtv.com/news/corporates/article-rbi-fines-2-co-operative-banks-under-anti-money-laundering-rules-1211713>> accessed 25 December 2015.

²³ International Monetary Fund (IMF), *Financial Systems Stability Update* (IMF Country Report No. 13/8, January 2013) 37.

related PEPs controls, which are not even clearly defined and explained in the RBI guidelines.

Why the definition of PEPs should be expanded in India

As argued earlier in this paper, in all the jurisdictions, it is critical for financial institutions to conduct greater scrutiny of business relationships with PEPs in order to deny corrupt PEPs access to the financial system and thereby address the potential corruption and money laundering risks associated with these customers. However, this becomes much more imperative for countries who have a strong background of grand corruption or misuse of public assets. Certainly, all PEPs are not corrupt, but it cannot be ignored that all PEPs are potentially in a position to abuse their positions for personal gain – no matter their country of origin (domestic or foreign PEPs), nature of business activities or seniority of position ('senior' or 'low' ranking public officials).

According to the 2014 Transparency International Corruption Perception Index (CPI), India had a 38 CPI score which indicates a medium to high degree of public sector corruption as perceived by business people and country analysts. The CPI score ranges between 100 (very clean) and 0 (highly corrupt). Corruption is a known phenomenon in the public sector in India, which is arguably evidenced by several scandals involving public officials in the past few years. For instance, there were allegations of gross misappropriation of funds (estimated to be \$1.8 billion) at the 2010 Commonwealth Games, leading to the resignation of two senior political party members and other government officials. In 2008, an auditor's report uncovered a massive Telecom Scam (widely known as the '2G Scam') involving senior politicians, cabinet ministers and government officials, which was estimated to have costed the government nearly \$39 billion, making it one of the biggest cases of grand corruption in India's history.²⁴ Charges under the PMLA were filed for this scandal and many major arrests were made. The Enforcement Directorate of India (EDI) claimed that the 2G scam's money trail is linked to ten countries, clearly indicating the international ramifications of the case.²⁵ The argument of this paper is further supported by Global Financial Integrity (GFI) research, which places India as the decade's eighth largest exporter of illicit capital, losing US\$123 billion in black money from 2001 to 2010.²⁶

Clearly, all these scandals involve domestic PEPs, which, arguably, in light of the country's history of corruption and current scandals, should be included within the scope of the definition of PEPs. It is argued that banks, in compliance with the revised FATF Recommendations, should be required to adopt a risk-based approach in applying CDD measures to domestic PEPs and if there a higher risk in establishing or continuing a business

²⁴ 'Punishing Corruption in India: Taking License Raja' *The Economist* (Delhi, 18 November 2010) <http://www.economist.com/blogs/banyan/2010/11/punishing_corruption_india> accessed 25 December 2015.

²⁵ Reporter, 'Money trail in 2G spectrum scam covers 10 countries: ED' *Times of India* (8 December 2010) <<http://timesofindia.indiatimes.com/india/Money-trail-in-2G-spectrum-scam-covers-10-countries-ED/articleshow/7067801.cms>> accessed 25 December 2015.

²⁶ C. Gascoigne and E.J. Fagan, 'India loses US\$ 1.6 billion in black money in 2010, loses US\$ 123 billion from 2001-2010' (GFI Research, 17 December 2012) <<http://www.gfintegrity.org/press-release/india-loses-us1-6-billion-black-money-2010-loses-us123-billion-2001-2010/>> accessed 25 December 2015.

relationship with domestic PEPs is perceived, EDD measures must also be applied to domestic PEPs.

Similar to foreign PEPs, domestic PEPs are also in a position which they can easily exploit for their private profits, which then need to be laundered in different forms – for instance, by becoming the beneficial owner of a company, through their close associates, etc. – and thus, using the financial system to hide the origins of their illicit funds. Arguably, thus, there is no reason for distinguishing between foreign and domestic PEPs in India and for not applying similar EDD checks to the close associates of PEPs as well.

Conclusion

This paper clearly establishes that despite the revised FATF Recommendation relating to PEPs, including both the foreign and domestic PEPs within the scope of the PEP definition, no steps have been taken by the Indian jurisdiction to amend its current regulations to be in compliance with the revised FATF Recommendations. Arguably, the distinction made between foreign and domestic PEPs in India allows domestic PEPs, their close relatives and close associates to remain ‘off the book’ when there is no justifiable reason for making such a distinction – all PEPs (whether foreign or domestic) have an opportunity to misuse their position for personal gain and pose similar higher levels of risk for money laundering purposes. This paper argues that it is high time for India and RBI to issue proper guidelines on the concept of PEPs and to expand the definition of PEPs to include domestic PEPs and close associates of PEPs as well. It is argued that clear guidelines on the concept of PEPs need to be issued to banks so that the PEP regime in India can be made more effective and comply with the revised 2012 FATF Recommendations.